

STATE OF MICHIGAN  
IN THE SUPREME COURT  
APPEAL FROM COURT OF APPEALS  
Fitzgerald, P.J., and Neff and White, J.J.

ALBERTA STUDIER, PATRICIA M. SANOCKI,  
MARY A. NICHOLS, LAVIVA M. CABAY,  
MARY L. WOODRING, AND  
MILDRED E. WEDELL,

Plaintiffs-Appellees,

Supreme Court No. 125766

v

Court of Appeals No. 243796

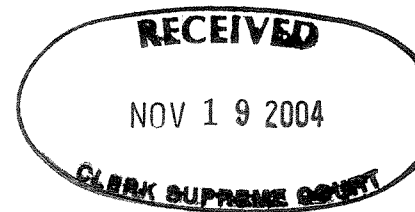
MICHIGAN PUBLIC SCHOOL EMPLOYEES'  
RETIREMENT BOARD, MICHIGAN PUBLIC  
SCHOOL EMPLOYEES' RETIREMENT  
SYSTEM, MICHIGAN DEPARTMENT OF  
MANAGEMENT AND BUDGET, AND  
TREASURER OF THE STATE OF MICHIGAN,

Ingham County Circuit Court  
No. 00-92435-AZ

Defendants-Appellants,

\_\_\_\_\_ /

**APPELLANTS' BRIEF ON APPEAL**  
**ORAL ARGUMENT REQUESTED**



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## **QUESTION PRESENTED FOR REVIEW**

- I. MCL 38.1391(1) directs the Michigan Public School Employees' Retirement System to "pay the entire monthly premium or membership or subscription fee for hospital, medical-surgical and sick care benefits for the benefit of a retirant or retirement allowance beneficiary who elects coverage in the plan authorized by the retirement board and the department." Since MCL 38.1391(1) does not contain any language that a contract was intended, does MCL 38.1391(1) create a contractual obligation for health benefits?**

The Defendants-Appellants' answer: "No"

The Plaintiffs-Appellees' answer: "Yes"

The Trial Court answered: "Yes"

The Court of Appeals answered: "Yes"

## **INTRODUCTION**

This case involves section 91(1), MCL 38.1391(1), of the Michigan Public School Employees Retirement Act of 1979, 1980 PA 300, MCL 38.1301, *et seq* (Act). (Defendants' Appendix 110a) Plaintiffs-Appellees (Plaintiffs) are six retired members of the Michigan Public School Employees Retirement System (MPERS) who claim that MCL 38.1391(1) created "contractual rights for public school employees" for health benefits. Plaintiffs alleged that Defendants-Appellants' (Defendants) increase in health insurance deductibles (deductibles), and prescription drug co-payments (co-pays), implemented January 1, 2000 and April 1, 2000, respectively, to the Master Health Care Plan (Plan) (2000 Modifications) violated Const 1963, art 1, § 10, and US Const, art I, § 10. Plaintiffs also alleged that the 2000 Modifications to the Plan violated Const 1963, art 9, § 24, which prohibits the impairment of "accrued financial benefits." Plaintiffs requested issuance of a preliminary and permanent injunction, and an order to reinstate the deductibles and co-pays in effect prior to January 1, 2000 and April 1, 2000, respectively.

The Legislature first provided for health benefits for retirees of MPERS in 1974 when it granted the Michigan Public School Employees' Retirement Board (Board) and the Department of Management and Budget (Department)<sup>1</sup> the authority to authorize a plan for health benefits. 1974 PA 244, §§ 25b and 27e. (Defendants' Appendix 99a and 104a-105a) 1974 PA 244 further provided that the Board pay a maximum of \$25.00 per month for the benefit of any retiree who elected coverage in an authorized plan. In 1975, the Board and the Department authorized a plan that provided a 10% co-payment by retirees on selected medical services and all covered

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<sup>1</sup> Department is defined in MCL 38.1304(4) to mean the Department of Management and Budget.

prescription drugs. Since 1974, the legislation giving the Board and the Department the authority to authorize the Plan has been amended numerous times. In addition, the Board and the Department have modified the Plan to include a multitude of new medical procedures and prescription drugs that were not available in 1974, as well as changing the co-pay and deductible amounts payable by retirees. (Defendants' Appendix 65a-76a)

Defendants filed a Motion for Summary Disposition that the Trial Court granted on August 29, 2002. In an opinion issued February 3, 2004, the Court of Appeals held that MCL 38.1391(1) created a contract, but found that the 2000 Modifications did not impair that contract. The Court also held that health care benefits were not "accrued financial benefits" as that phase is used in Const 1963, art 9, § 24. (Defendants' Appendix 12a) The Supreme Court granted Defendants' Application for Leave to Appeal that challenged the Court of Appeals' decision which found that MCL 38.1391(1) created a contract.

Defendants only address the issue of whether MCL 38.1391(1) created a contract for health benefits in this brief. The issue of whether the challenged health care plan amendments impair existing contractual obligations in violation of Const 1963, art 1, § 10, US Const, art I, §10 and Const 1963, art 9, § 24 will be addressed by Defendants-Appellees in *Studier v Michigan Public School Employees' Retirement Bd*, Docket No. 125765.

MCL 38.1391(1) does not create a contract. It does not contain any words that establish a contract, such as "contract," "agreement," or "promise." It is clear from the language used in MCL 38.1391(1) that the Legislature never intended to create a contract when it enacted MCL 38.1391(1) because MCL 38.1391(1) is significantly different from the language used in other statutes where the Legislature did intend to create a contract. Furthermore, a reasonable construction of MCL 38.1391(1) establishes that it does not create a contract but instead

represents the current legislative policy, and that legislative policy has changed many times since 1974. The Legislature did not covenant in MCL 38.1391(1) that it would not amend the statute, as would be required when creating a contract. To the contrary, it has never so covenanted and, in fact, has amended the statute many times. Moreover, there is no indication whatsoever that when the Legislature enacted MCL 38.1391(1) it intended to bind future Legislatures and prevent them from utilizing their constitutional powers to amend the law. Finally, MCL 38.1391(1) is not a contractual obligation for health benefits because when it was enacted by the Legislature it did not manifest a clear intent to create rights protected by the Contract Clause.

This case affects more individuals than just the six<sup>2</sup> named Plaintiffs. MPSERS paid over \$370,000,000.00 in 2000 for retiree health care costs. (Defendants' Appendix 85a) Between 1993 and 2000 this cost almost doubled (*Id.*) and is projected to increase significantly in each of the foreseeable years.<sup>3</sup> If this Court finds that MCL 38.1391(1) created a contract that prohibits the Board and the Department from modifying the Plan to increase deductibles and co-pays, it will increase MPSERS' annual costs by millions of dollars. MPSERS will increase its assessments to schools to fund those costs, thus reducing the funds available for the education of the State's students.<sup>4</sup> In addition, if this Court finds that MCL 38.1391(1) creates a contract it will establish a precedent such that similar language in other retirement statutes and ordinances might be found to create contracts. That could increase the costs paid by the State and local governments for retiree health benefits. Thus, this Court should reverse that portion of the decision of the Court of Appeals that held that MCL 38.1391(1) created a contract and affirm the remainder of that opinion.

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<sup>2</sup> Mary A. Nichols died during the litigation and so is not analyzed here.

<sup>3</sup> See Citizens Research Council of Michigan, Financing Michigan Retired Teacher Pension and Health Care Benefits, Report 337, <http://www.crcmich.org> (September 2004).

<sup>4</sup> *Id.*

## **STATEMENT OF PROCEEDINGS AND FACTS**

### **Procedural Facts**

On October 2, 2000, the Plaintiffs filed a three-count amended complaint. Count I alleged the Defendants violated Const 1963, art 9, § 24 by increasing Plaintiffs' prescription drug co-payments and the deductibles in the Plan authorized by the Board. Count II alleged the Defendants violated Const 1963, art 1, § 10 and US Const, art I, §10 by increasing Plaintiffs' prescription drug co-payments and the deductibles in the Plan. Count III alleged that all Defendants violated their trust and fiduciary duties owed to Plaintiffs by implementing a Plan that increased prescription drug co-payments and the deductibles in the Plan.<sup>5</sup>

On February 21, 2001, the trial court issued an order finding that the Plan did not violate Const 1963, art 9, § 24:

Since both the Michigan Court of Appeals and Michigan Supreme Court have been squarely faced with the opportunity to rule on this question and have declined to do so, this Court cannot rule that health benefits constitute 'accrued financial benefits' under Article IX, section 24. [Defendants' Appendix 25a]

On August 28, 2001, after the parties filed briefs on the state and federal contract impairment clause, the court issued a second opinion reiterating that health benefits do not constitute "accrued financial benefits" as described in Const 1963, art 9, § 24. The Court also rejected Plaintiffs' argument that any payment less than the full monthly premium constitutes an impairment and denied the Plaintiffs' motion for preliminary injunction. (Defendants' Appendix 43a-46a)

Plaintiffs and Defendants filed Motions for Summary Disposition and Briefs in support on December 17, 2001, and reply briefs on January 18, 2002. On August 29, 2002, the trial court

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<sup>5</sup> Count III was not pursued by the Plaintiffs in the Court of Appeals, so it has been abandoned. *Mitcham v City of Detroit*, 355 Mich 182, 203; 94 NW2d 388 (1959); *Mudge v Macomb County*, 458 Mich 87, 105; 580 NW2d 845 (1998).

issued its final order granting Defendants' Motion for Summary Disposition and dismissing Plaintiffs' action. (Defendants' Appendix 15a-21a)

On September 16, 2002, Plaintiffs appealed the circuit court's decision to the Court of Appeals. The Court of Appeals, on February 3, 2004, issued an opinion affirming the circuit court order granting Defendants' Motion for Summary Disposition, pursuant to MCR 2.116(C)(10). However, the Court of Appeals held that MCL 38.1391(1) created a contractual obligation to provide health insurance that is subject to federal and state contract impairment clauses. US Const, art I, § 10; Const 1963, art 1, § 10. (Defendants' Appendix 4a-14a). *Studier v MPSEERS*, 260 Mich App 460, 476; 679 NW2d 88 (2004).

On March 15, 2004, Defendants filed an Application for Leave to Appeal to this Court challenging the Court of Appeals' holding that MCL 38.1391(1) created a contractual obligation.<sup>6</sup> (Supreme Court Docket No. 125766) On September 16, 2004, this Court issued an Order granting the Defendants' Application for Leave. This Court directed the parties to include, among the issues briefed:

[W]hether the health benefits described in MCL 38.1391(1) are a contractual obligation that cannot be diminished or impaired by the state. Const. 1963, art 1, § 10, and US Const, art I, § 10.

The Court further ordered that this case be argued and submitted together with *Studier v Michigan Public School Employees' Retirement Bd*, Docket No. 125765.

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<sup>6</sup> On March 15, 2004, Plaintiffs also filed an Application for Leave to Appeal to this Court, (Supreme Court Docket No. 125765) on other grounds. That application was also granted on September 16, 2004.

## **Substantive Facts**

### **1. Legislative History of MCL 38.1391(1)**

MPERS did not pay for any health benefits for its retirees until passage of 1974 PA 244. 1974 PA 244 amended 1945 PA 136 by adding MCL 38.227e(1) and 38.325b(1)<sup>7</sup>, that contain the following language:

On or after January 1, 1975, hospitalization and medical coverage insurance premium payable by a retirant or his beneficiary and his dependants, not to exceed \$25.00 per month, under any group plan authorized by the retirement board [commission] created under this chapter and the department of management and budget shall be paid by the retirement board [commission] from appropriations for this purpose made to the pension accumulation fund. . . . The payment shall not be made unless the retirant or beneficiary elects coverage under a group plan authorized under this section.

The original monthly premium amount in MCL 38.227e(1) and 38.325b(1) has been amended several times.<sup>8</sup>

The first major change in the statute occurred when Section 107 of 1980 PA 300, repealed 1945 PA 136 and replaced it with the Public School Employees Retirement Act of 1979, MCL 38.1301 *et seq.* Section 91 of the Act, MCL 38.1391(1), now contains the provisions for health benefits for retirees. The premium amount in MCL 38.1391(1) continued to be increased.<sup>9</sup> The language in section 91(1) significantly changed with the passage of 1983 PA 143, which deleted a fixed dollar amount for the monthly premium. For comparative purposes, the new language, as of 1983, is underlined:

The retirement system shall pay the entire monthly premium, in the amount

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<sup>7</sup> Chapter 1 of 1945 PA 136, as amended, included MCL 38.227e and created a retirement system for all Michigan "public school employees", as defined in that chapter. However, Chapter 1 did not apply to school districts of the first class. 1945 PA 136, as amended, MCL 38.231. Chapter 2 of 1945 PA 136, as amended, included MCL 38.325b and created a retirement system for employees of the board of education of school districts of the first class.

<sup>8</sup> 1978 PA 470 increased the amount to \$31.00, 1979 PA 60 increased it to \$40.00.

<sup>9</sup> 1981 PA 133 increased the amount to \$52.00, 1982 PA 258 increased it to \$66.00.

authorized by the legislature, for hospital, medical-surgical, and sick care benefits for the benefit of a retirant or retirement allowance beneficiary who elects coverage in the group health insurance or prepaid service plan authorized by the retirement board and the department; and may pay up to the maximum of that amount toward the monthly premium for hospital, medical-surgical, and sick care benefits for the benefit of a retirant or retirement allowance beneficiary enrolled in another group health insurance or prepaid service plan, if enrolled prior to June 1, 1975 and for whom the retirement system on the effective date of this 1983 amendatory act was making a payment towards his or her monthly premium. A retirant or retirement allowance beneficiary until eligible for medicare shall have an amount equal to the cost chargeable to a medicare recipient for part B of medicare deducted from his or her retirement allowance.

MCL 38.1391(1) was amended several more times.<sup>10</sup> In September 2000, when Plaintiffs

filed their complaint, MCL 38.1391(1) provided:

The retirement system shall pay the entire monthly premium, or membership or subscription fee for hospital, medical-surgical, and sick care benefits for the benefit of a retirant or retirement allowance beneficiary who elects coverage in the plan authorized by the retirement board and the department.<sup>11</sup> [Defendants' Appendix 110a-111a]

## **2. History of the Michigan Public School Employees' Retirement System**

MPSERS is a statewide, public school employee retirement system that provides a cost-sharing Plan for approximately 144,000 retirees and their dependents. The Plan has been self-insured since January 1, 1992. As a self-insured plan, MPSERS pays all claims after retirees pay their co-pays and deductibles. MPSERS has engaged Blue Cross Blue Shield of Michigan (BCBSM) to administer the Plan. Since its inception in 1975 the Plan has included cost-sharing features such as the monthly premium subsidy, deductibles, and co-pays on selected medical services and prescription drugs. (Defendants' Appendix 65a-76a) Since 1975 numerous benefit changes have been made to the Plan, such as including coverage for more medical procedures,

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<sup>10</sup> 1985 PA 91; 1989 PA 193; 1996 PA 488; and 1997 PA 143.

<sup>11</sup> MCL 38.1391(1) has not been amended since 1997.

prescriptions, and services, as well as instituting cost-sharing adjustments. (Defendants'

Appendix 67a-76a)

**a) Deductibles**

The individual and family deductible component of the Plan gradually increased from 1982 to 2000:

<b>YEAR</b>	<b>PER PERSON</b>	<b>PER FAMILY</b>
1982-1991	\$ 50	\$100
1992-1994	\$ 80	\$160
1995-1996	\$ 95	\$190
1997-1998	\$125	\$250
1999	\$145	\$290
2000	\$165	\$330

(Defendants' Appendix 67a-76a)<sup>12</sup>

**b) Prescription Drug Co Pays**

The prescription drug program also had gradual changes between 1975 and March 31, 2000:

<b>Year</b>	<b>Co-pay</b>		<b>Mail Order Plan/Co-pay</b>	<b>Maximum Out of Pocket Co-pay</b>
1975-1983	10% all covered drugs			No Limit
10/1/83-1991	\$3.00 per prescription all covered drugs			No Limit
1/1/92	\$4.00 all covered drugs			No Limit
1/1/94	No change to co-pay		New mail order prescription program - 90 day supply for 1 co-pay	No Limit
1/1/97	Implement dual-tier prescription program			No Limit
	Generic	Brand Name		No Limit
1/1/97-3/31/00	\$4.00	\$8.00		

(Defendants' Appendix 67a-76a)

<sup>12</sup> The total costs to provide the health benefit plan almost doubled from 1993 to 2000. (Defendants' Appendix 85a)

The prescription drug co-payment benefit was changed effective April 1, 2000:

Year	Retail Co-pay	Mail Order Co-pay	Maximum Out of Pocket Co-pay
4/1/00	20% co-pay, \$4 minimum and \$20 maximum up to a one-month supply	20% co-pay, \$10 minimum and \$50 maximum up to a 90-day supply	Individual prescription drug out of pocket co-pay max. per calendar year is \$750.00 [2000 – <i>pro-rated to \$560.00</i> ]
1/1/01	Formulary implemented. Purchase of non-formulary drug requires additional 20% co-pay, not subject to maximum.		

(Circuit Court Docket Entry 120, Exhibit A, pp 5-6)

The Plaintiffs alleged that the increase in yearly deductibles from \$145 to \$165 per person and from \$290 to \$330 per family, along with the changes to the co-pays for prescription drugs, violated Const 1963, art I, § 10 and art 9, § 24.

### 3. Funding Payment of Premiums

If the Board and the Department authorize a Plan and a retiree<sup>13</sup> elects to participate in the Plan, MCL 38.1391(1) provides that MPSERS pay the monthly premium for the Plan. The cost of the Plan is financed by school districts on a pay-as-you-go basis. Pursuant to MCL 38.1341(1)-(2), MPSERS must annually determine the amount needed to pay for the pension and health care costs of retirees. The aggregate compensation estimated to be paid to public school employees is also determined. MCL 38.1341(3). The Director of the Department then certifies the amount due from reporting units<sup>14</sup> as required by MCL 38.1341(4) for the cost of pensions and retiree health care benefits. MCL 38.1341(5) then requires the reporting units to make

<sup>13</sup> MPSERS provides health benefits for employees who retire before age 65. When a member becomes Medicare eligible (65 yrs), the MPSERS Plan becomes secondary and coverage is coordinated with Medicare. See MCL 38.1391(9).

<sup>14</sup> MCL 38.1307(3) defines reporting unit to include "public school district, intermediate school district, public school academy, tax supported community or junior college, or university, or an agency having employees on its payroll who are members of this retirement system."

payment of the amounts certified by the Director of the Department. The percentage of compensation that is required to be paid to MPSERS for health benefits has steadily increased from 1.25% in 1985 to 5.55% in 2001. (Defendants' Appendix 79a) The percentage is projected to increase to 19.9% in 2020.<sup>15</sup> This means that, without any changes in deductible and co-pays, health care costs will increase so that by 2020 almost 20% of the aggregate compensation paid to public school employees will have to be paid to MPSERS to pay retiree health care costs. Without the changes in 2000, health care costs would be even higher by 2020.

Public school districts (reporting units) receive their revenue mainly from two sources: local property taxes and state appropriations made in the State School Aid Act, MCL 388.1601 *et seq.* The vast majority of the money that the Legislature appropriates in the State School Aid Act is transferred from the State School Aid Fund created by Const 1963, art 9, § 11. The State School Aid Fund is comprised of sales taxes, a six mill state-wide tax on all real and personal property (MCL 211.903), and other state revenue. *Durant v State of Michigan*, 238 Mich App 185, 195-198; 605 NW2d 66 (1999). MCL 388.1620 provided a basic foundation allowance to each school district of \$6,000 for 2000-2001, \$6,300 for 2001-2002 and \$6,700 per pupil for years 2002-2003, 2003-2004 and 2004-2005. *Durant v State of Michigan*, 251 Mich App 297, 300-302; 650 NW2d 380 (2002). Thus, while the amount increased between 2000 and 2002, the amount of money provided by the state to school districts for each pupil has not increased in three years.

School districts are now limited, with voter approval, to a maximum levy of 18 mills or the number of local school operation mills levied in 1993, whichever is less, on real property. MCL 380.1211. However, homestead and qualified agricultural property is exempt from the 18

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<sup>15</sup> See [www.crcmich.org](http://www.crcmich.org): Report 337, September 2004, Financing Michigan Retired Teacher Pension and Health Care Benefits, a publication of the Citizens Research Council of Michigan.

mill levy. MCL 211.7cc, 380.1211e. See *Citizens for Uniform Taxation v Northport Public School*, 239 Mich App 284, 286; 608 NW2d 480 (2000). In some instances schools may also assess a Hold Harmless Millage with voter approval of 3 mills for school operation purposes. MCL 380.1211c and MCL 380.705

Thus, the cost to school districts for providing health benefits is increasing while the revenue received by school districts is generally remaining constant.

## ARGUMENT

### **I. MCL 38.1391(1) does not create a contract to provide health benefits for retirees of the Michigan Public School Employees' Retirement System.**

#### **A. Standard of Review**

Questions requiring statutory interpretation are reviewed *de novo*. *Rakestraw v General Dynamics Land Systems, Inc.*, 469 Mich 220, 224; 666 NW2d 199 (2003). Constitutional issues are also reviewed *de novo*. *McDougall v Schanz*, 461 Mich 15, 24; 597 NW2d 148 (1999).

This Court, in *Rakestraw*, 469 Mich at 224, set forth the standard for interpreting a statute as follows:

In interpreting a statute, our obligation is to discern the legislative intent that may reasonably be inferred from the words actually used in the statute. *White v Ann Arbor*, 406 Mich 554, 562; 281 NW2d 283 (1979). A bedrock principle of statutory construction is that "a clear and unambiguous statute leaves no room for judicial construction or interpretation." *Coleman v Gurwin*, 443 Mich 59, 65; 503 NW2d 435 (1993). When the statutory language is unambiguous, the proper role of the judiciary is to simply apply the terms of the statute to the facts of a particular case. *Turner v Auto Club Ins Ass'n*, 448 Mich 22, 27; 528 NW2d 681 (1995). In addition, words used by the Legislature must be given their common, ordinary meaning. MCL 8.3a.

This Court has also held that a court may read nothing into an unambiguous statute that is not within the manifest intent of the Legislature as derived from the words of the statute itself. *Omne Financial, Inc v Shacks*, 460 Mich 305, 311; 596 NW2d 591 (1999).

#### **B. A statute creates a contract only if: the Legislature has unambiguously expressed an intention to create an obligation; the statute is susceptible of no other reasonable construction; the Legislature covenants that it will not be amended; and the statute does not surrender an essential attribute of the State's sovereignty.**

The United States Supreme Court, in *National Railroad Passenger Corporation v Atchison, Topeka & Sante Fe Railway Co*, 470 US 451, 465-466; 105 S Ct 1441; 84 L E2d 432 (1985) held that absent a clear indication that the Legislature intends to bind itself contractually,

the law presumes that the Legislature has merely declared a policy to be pursued until the Legislature shall ordain otherwise:

For many decades, this Court has maintained that absent some clear indication that the legislature intends to bind itself contractually, the presumption is that a "law is not intended to create private contractual or vested rights but merely declares a policy to be pursued until the legislature shall ordain otherwise." *Dodge v. Board of Education*, 302 U.S. 74, 79 (1937). See also *Rector of Christ Church v. County of Philadelphia*, 24 How. 300, 302 (1861) ("Such an interpretation is not to be favored"). This well-established presumption is grounded in the elementary proposition that the principal function of a legislature is not to make contracts, but to make laws that establish the policy of the state. *Indiana ex rel. Anderson v. Brand*, 303 U.S. 95, 104-105 (1938). Policies, unlike contracts, are inherently subject to revision and repeal, and to construe laws as contracts when the obligation is not clearly and unequivocally expressed would be to limit drastically the essential powers of a legislative body. Indeed, "[the] continued existence of a government would be of no great value, if by implications and presumptions, it was disarmed of the powers necessary to accomplish the ends of its creation." *Keefe v. Clark*, 322 U.S. 393, 397 (1944) (quoting *Charles River Bridge v. Warren Bridge*, 11 Pet. 420, 548 (1837)). Thus, the party asserting the creation of a contract must overcome this well-founded presumption, *Dodge, supra*, at 79, and we proceed cautiously both in identifying a contract within the language of a regulatory statute and in defining the contours of any contractual obligation.

In determining whether a particular statute gives rise to a contractual obligation, "it is of first importance to examine the language of the statute." *Dodge v. Board of Education, supra*, at 78. See also *Indiana ex rel. Anderson v. Brand, supra*, at 104 ("Where the claim is that the State's policy embodied in a statute is to bind its instrumentalities by contract, the cardinal inquiry is as to the terms of the statute supposed to create such a contract"). "If it provides for the execution of a written contract *on behalf of the state* the case for an obligation binding upon the state is clear." 302 U.S., at 78 (emphasis supplied). But absent "an adequate expression of an actual intent" of the State to bind itself, *Wisconsin & Michigan R. Co. v. Powers*, 191 U.S. 379, 386-387 (1903), this Court simply will not lightly construe that which is undoubtedly a scheme of public regulation to be, in addition, a private contract to which the State is a party. [Emphasis added]

Based upon this standard, the Supreme Court held that the Rail Passenger Service Act of 1970, 45 USC §501 *et seq.*, did not create a contract because it did not contain any Congressional intent to do so.

The United States Supreme Court has further held that the "reserved powers doctrine" provides that a state contract is void *ab initio* if it "surrenders an essential attribute of its sovereignty," since a "legislature cannot bargain away the police power of a state." *United States Trust Co v New Jersey*, 431 US 1, 23; 97 S Ct 1505; 52 L Ed2d 92 (1977). Additionally, "measures or engagements adopted or undertaken by the body politic or State government for the benefit of all, and from the necessity of the case, and according to universal understanding, to be varied or discontinued as the public good shall require" are not contracts protected by US Const, art I, § 10. *Butler v Commonwealth of Pennsylvania*, 51 US 402, 416; 10 HOW 402; 13 L Ed 472 (1851). Finally, a State has the right to "enact and repeal laws" unless specifically restricted by the Constitution. *Id.* at 417.

This Court has similarly held that no contract is created by a statute unless the language employed therein is plain and susceptible of no other reasonable construction than that the Legislature intended to be bound by a contract. In *In re Certified Question*, 444 Mich 765, 777-778; 527 NW2d 468 (1994) *cert den* 514 US 1127 (1995):

"Courts usually have concluded that a state contractual obligation arises from legislation only if the legislature has unambiguously expressed an intention to create the obligation." In order to prove that a statutory provision has formed the basis of a contract, the language employed in the statute must be "plain and susceptible of no other reasonable construction" than that the legislature intended to be bound to a contract. As a general rule, vested rights are not created by a statute that is later revoked or modified by the legislature if "the legislature did not covenant not to amend the legislation." Yet, a statute can create a contract if the language and circumstances demonstrate a clear expression of legislative intent to create private rights of a contractual nature enforceable against a state. [citations omitted].

In the case of *In re Certified Question*, *supra*, the plaintiffs claimed that the Worker's Disability Compensation Act, MCL 418.101 *et seq.*, created a contractual relationship with policyholders so that any surplus in the Workers' Compensation Fund must be distributed to the

policyholders. This Court analyzed the statute and concluded that there was no clear expression of legislative intent to create a contract. Instead, the Court found that the language was just an expression of general policy and was not a covenant between the state and policyholders. *Id.* at 784-785.

This Court rejected a claim of contractual entitlement in *Romein v General Motors*, 436 Mich 515; 462 NW2d 555 (1990), where the defendants claimed that the retroactive provisions in 1987 PA 28, §354(17)-(20), (that amended the Worker's Disability Compensation Act) violated Const 1963, art 1, § 10 and US Const, art I, § 10, because they revived liabilities of employers that were fully discharged by completed transactions in reliance on state law. The Court held this contention lacked merit, primarily because such an expectation was not protected by the Contract Clause:

The defendants cannot rely on the level of benefits existing at the time of an injury as a legitimate contractual expectation protected by the Contract Clause. *Lahti, supra* at 590-592. [*Romein*, 436 Mich at 533.]

In *Franks v White Pine Copper*, 422 Mich 636; 375 NW2d 715 (1985), the Court characterized worker's compensation benefits as social-welfare, income-maintenance benefits. The Court further noted that this program, like other income maintenance programs that provide benefits, is funded by impositions on employers and others of mandatory payments with statutorily prescribed benefits. 422 Mich at 654. The Court also stated, "In providing for such benefits, the Legislature did not covenant not to amend the legislation." 422 Mich at 654. As a result, benefits could be changed by future legislation.

Other Courts have likewise held that a statute must contain clear and unequivocal language that the Legislature has intended to create a contract. In *National Education Ass'n – Rhode Island v Retirement Board*, 172 F3d 22, 24 (CA 1, 1999), the Rhode Island Legislature

passed a law to amend its retirement system to allow employees of the state's teacher union to join the system and purchase service credit for a modest fee for the years employed by the union. This allowed union employees to immediately retire with pension allowances in excess of their contributions. When the effect of the law was realized, it was repealed. The Legislature then passed 1994 R.I. Pub. Laws ch. 413, §1 to terminate the pensions of those union employees who had entered the system under the repealed statute. Rhode Island's general pension law, R.I. Gen Laws § 36-10-7, under which the union employees claimed their retirement, stated:

[I]t is the intention of the state to make payment of the annuities, benefits, and retirement allowances provided for under the provisions of this chapter and...to make the appropriations required by the state to meet its obligations to the extent provided in this chapter. The general assembly shall make annual appropriations which shall be sufficient to provide for the payment of annuities, benefits, and retirement allowances required of the state under this chapter.

The Court, in *National Education Ass'n*, 172 F3d at 28, found that this statutory language did not create a contract:

We do not think that the Rhode Island general pension statute "clearly and unequivocally" contracts for future benefits either by language or – in the circumstances of this case – through the nature of the relationship. Nowhere does the statute call the pension plan a "contract" or contain an anti-retroactivity clause as to future changes.

As a result, the Court found that 1994 R.I. Pub. Laws ch. 413, §1 did not violate the Contract Clause, US Const, art 1, § 10.

In *Spiller v State of Maine*, 627 A2d 513, 514; (1993), the Maine Legislature created a retirement system to which both employees and the State were required to contribute. In 1992, the State had a shortfall in revenue and, to reduce expenditures, amended the retirement statute to lower the prospective retirement benefits of all state employees with less than seven years of service. The plaintiffs alleged that this statutory change violated the Contract Clauses of the Maine and the United States Constitutions. Relying on *National Railroad Passenger Corp*,

*supra*, the Maine Supreme Court held that no contract had been established by the Legislature because there was "no clear indication of a legislative intent to create immutable contracted rights for all State employees." 627 A2d at 516. See also *Parker v Wahelin*, 123 F3d 1 (CA 1, 1997), *United States RR Retirement Bd v Fritz*, 449 US 166, 173; 101 S Ct 453; 66 L Ed2d 368; (1980) and *Van Slooten v Larsen*, 410 Mich 21, 39-41; 299 NW2d 704 (1980) *app dis* 455 US 901, 102 S Ct 1242; 71 L Ed2d 440.

Thus, a statute does not create a contract unless the Legislature has clearly and unambiguously expressed an intention to create a contractual obligation; the statute is susceptible of no other reasonable construction; the Legislature covenants that the statute will not be amended; and the statute does not surrender an essential attribute of the State's sovereignty.

C. MCL 38.1391(1) does not create a contract because it does not meet the criteria established by the Courts.

MCL 38.1391(1) provides that the Board and the Department may authorize a Plan for hospital, medical-surgical and sick care benefits for retirees and, if so authorized, MPSERS shall pay the premium or membership or subscription fee for the plan:

The retirement system shall pay the entire monthly premium or membership or subscription fee for hospital, medical-surgical, and sick care benefits for the benefit of a retirant or retirant allowance beneficiary who elects coverage in the plan authorized by the retirement board and the department.

This language, however, does not create a contractual obligation between the MPSERS and retirees for health benefits because it does not contain an express intention to create an obligation; it is susceptible of another reasonable construction; it does not covenant that it will not be amended; and it does surrender an essential attribute of the State's sovereignty, the right to spend limited tax dollars. As a result, this Court should reverse that portion of the Court of Appeals' decision that holds otherwise. See *Studier*, 260 Mich App at 476.

The plain language of MCL 38.1391(1) does not establish that the Legislature intended to be bound to a contract. First, MCL 38.1391(1) allows the Board and the Department to authorize a Plan for health care coverage, but there is no requirement that a Plan be authorized. Second, retirees are not automatically participants in an authorized Plan; they must elect to be covered by the Plan. Third, the statute requires MPSERS to pay the entire monthly premium or membership or subscription fee only if a Plan is authorized and a retiree elects to participate. This language does not state that the Legislature was creating a contract with retirees. In fact, the words "contract," "covenant," or similar words do not appear in MCL 38.1391(1). Furthermore, the Legislature did not say that MCL 38.1391(1) would never be amended or that the Board and the Department could not change the Plan.

The presumption is that, absent a clear indication by the Legislature of an intent to create a contract, a statute is merely a declaration of policy to be pursued. *Dodge v Board of Education*, 302 US 74, 79; 58 S Ct 98; 82 LEd 57 (1937). MCL 38.1391(1) gives the Board and the Department the ability to "authorize" a Plan. Authorize means "to empower; to give a right or authority to act."<sup>16</sup> MCL 38.1391(1) gives the Board and the Department a permissive grant of power. In other words, the Legislature's grant of discretion to the Board and the Department to authorize a Plan, evidences a Legislative intent to declare a policy to be pursued, not an intent to create a contract with retirees because MCL 38.1391(1) does not even require that a Plan be authorized.<sup>17</sup>

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<sup>16</sup> Black's Law Dictionary Revised Fourth Edition. Dictionary definitions are permitted when the statute doesn't contain a definition. MCL 38.1301 *et seq.*, does not contain a definition for "authorize." *Popma v Auto Club Ins Ass'n*, 446 Mich 460, 470; 521 NW2d 831 (1994).

<sup>17</sup> If the Legislature had intended that MPSERS pay all of a retiree's health care costs even if no Plan was authorized, the language giving the Board the power to authorize a plan would be meaningless, contrary to the rules of statutory construction. *Altman v Meridian Twp*, 439 Mich 623, 635; 487 NW2d 155 (1992).

A reasonable construction of MCL 38.1391(1) is that the current policy of the Legislature is to have MPSERS pay the premium for a retiree who elected the Plan "authorized" by the Board and the Department. This policy decision of the Legislature allows the Board and the Department to change the Plan as circumstances change, such as when new medical procedures and prescription drugs became available and costs of the Plan have changed.

The language in MCL 38.1391(1) gives the Board and the Department the discretion and ability to create a Plan to suit the circumstances. The statute did not prohibit the Board and the Department from changing the Plan after it was first adopted; otherwise the Board and the Department could not have changed the Plan over the years to incorporate medical advancements and to increase benefits to include hundreds of new medical procedures and prescription drugs. (Defendants' Appendix 65a-76a) Thus, this language does not create a contractual obligation for health benefits because the Legislature reasonably delegated the discretion to the Board and the Department to implement a health care plan that is capable of responding to changing conditions.

The Legislature first addressed payment for health benefits in 1974 PA 244, adding sections 27e and 25b as amendments to 1945 PA 136, the public school employees' retirement statute in effect at that time. This public act was amended by 1978 PA 470 and 1979 PA 60. In 1980, the Legislature repealed the former school retirement statute, 1945 PA 136; MCL 38.201 to 38.366 and replaced it with 1980 PA 300, MCL 38.1301 *et seq.* Section 91(1) of 1980 PA 300, MCL 38.1391 continued to provide for a plan for health care coverage for retirees. Since the Legislature amended MCL 38.1391(1) by 1981 PA 133, 1982 PA 258, 1983 PA 143, 1985 PA 91, 1989 PA 193, 1996 PA 488 and 1997 PA 143, it clearly did not intend MCL 38.1391(1) to create a contract. In other words, if the Legislature intended MCL 38.1391(1) to create a contract, it would have included a covenant in MCL 38.1391(1) that it would not be amended.

The Legislature did not declare a policy to pursue health insurance for public school retirees until 1975 and then only certain hospital, medical and surgical procedures were included. Over the years, MCL 38.1391(1) was amended many times to alter the amount of the premium to be paid by MPSERS. Additionally, the Plan co-pays and deductibles were increased by the Board and the Department. With so many changes to the Plan between 1975 and 2000, it cannot be said that Petitioners had any expectation that the benefits provided by MCL 38.1391(1) created rights protected by the Contract Clause.

Plaintiffs began work with their respective public school districts well before the enactment of 1974 PA 244 and of MCL 38.1391(1) in 1980.<sup>18</sup> Their contract of employment was with their individual school district. Thus, health benefits could not have been an element of consideration for employment. Moreover, the Plaintiffs knew or should have known that coverage for health benefits could change since the Legislature amended 1974 PA 244 and MCL 38.1391(1) numerous times. Thus, it is apparent that health benefits for retirees could not have been a part of any contract of employment or an element of consideration in exchange for services rendered.

MCL 38.1391(1) simply does not contain any language that the Legislature will make the appropriations necessary to satisfy MPSERS' obligation to provide health benefits to retirees. Thus, it cannot be concluded here that MCL 38.1391(1) creates a contract because to do so would surrender an essential attribute of Michigan's sovereignty, i.e., the right of future Legislatures to determine how to spend limited revenues.

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<sup>18</sup> Plaintiff Alberta Studier began employment with the public schools about 1947. Plaintiff Patricia Sanocki began employment with the public schools about 1969. Plaintiff Laviva Cabay began employment with the public schools about 1970. Plaintiff Mary Woodring began employment with the public schools about 1961. Plaintiff Mildred Wedell began employment with the public schools about 1953. Mary A. Nichols died during the litigation and is not analyzed here. (Defendant's Appendix 51a-64a)

The elements of a traditional contract are: "parties competent to contract, a proper subject matter, legal consideration, mutuality of agreement, and mutuality of obligation." *Detroit Trust Co v Struggles*, 289 Mich 595, 599; 286 NW 844 (1939). As a result, "where mutual assent does not exist, a contract does not exist." *Quality Products v Nagel Precision*, 469 Mich 362, 372; 666 NW2d 251 (2003). Moreover, whether "a meeting of the minds occurred is judged by an objective standard, looking to the express words of the parties and to their visible acts." *Groulx v Carlson*, 176 Mich App 484, 491; 440 NW2d 644 (1989). In MCL 38.1391(1) the discretion to authorize a plan is given to the Board and participation by retirees is voluntary. No meeting of the minds occurred because the Legislature did not intend the words of MCL 38.1391(1) to establish a contract.

In interpreting a statute, the entire statute must be reviewed and the words used must be read together to give meaning to the statute. *G C Timmis & Co v Guardian Alarm Co*, 468 Mich 416, 421; 662 NW2d 710 (2003). MCL 38.1391(3), (7), and (8) support the conclusion that the Legislature did not intend to create a contract in MCL 38.1391(1) because those provisions require or allow retirees to pay for the cost of their health benefits rather than MPSERS being required to pay the "entire monthly premium" as set forth in MCL 38.1391(1).<sup>19</sup>

It is clear that the Legislature did not intend to create a contract in MCL 38.1391(1) because the language in that statute is significantly different from the language in other statutes where a contract was intended. For example, 1982 PA 259, MCL 12.61 *et seq.* provides for the payment of State notes and bonds issued pursuant to Const 1963, art 9, §§ 14, 15, and 16. MCL 12.62 requires the state treasurer to make the payments on the loans. MCL 12.64 clearly and unequivocally establishes that 1982 PA 259 creates a contract:

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<sup>19</sup> MPSERS does pay the entire monthly premium after it collects any amounts of premium due from retirees pursuant to MCL 38.1391(3), (7) and (8).

This act shall be deemed a contract with the holders from time to time of obligations of this state.

Section 34 of the State Housing Development Authority Act, 1966 PA 346, MCL 125.1434, by its plain language creates a contract where it provides that the State "pledges and agrees" with holders of notes and bonds issued by the Authority that the State will not alter the rights of the Authority to pay off the notes and bonds or impair the rights of the holder of the notes and bonds:

The state pledges and agrees with the holders of any notes or bonds issued under this act, that the state will not limit or alter the rights vested in the authority to fulfill the terms of any agreements made with the holders thereof, or in any way impair the rights and remedies of the holders until the notes or bonds, together with the interest thereon, with interest on any unpaid installments of interest, and all costs and expenses in connection with any action or proceeding by or on behalf of such holders, are fully met and discharged. The authority is authorized to include this pledge and agreement of the state in any agreement with the holders of such notes or bonds. [Emphasis added]

Similar language was used by the Legislature in the Higher Education Facilities Authority Act, 1969 PA 295, MCL 390.921 *et seq.*, and the recently enacted Michigan Broadband Development Authority Act, 2000 PA 49, MCL 484.3201 *et seq.* See MCL 390.927 and 484.3216, respectively.

Thus, it is clear that when the Legislature intended to create contracts, both before and after the enactment of MCL 38.1391(1) in 1980 PA 300, it did so using very specific language. Since the Legislature did not use similarly specific language in MCL 38.1391(1), it is evident that the Legislature did not intend to create a contract by enacting MCL 38.1391(1). Moreover, a reasonable construction of MCL 38.1391(1) is that the Legislature established a policy to pay for health care benefits as those benefits are authorized by the Board and the Department. Furthermore, since the Legislature did not state that MCL 38.1391(1) would never be amended, it did not enter into a contract with retirees. Finally, the Legislature could not make a contract to

forever pay for health care benefits when to do so would give up an essential attribute of sovereignty; the right to determine how to spend limited state tax revenues.

D. The Court of Appeals Erred When It Concluded That MCL 38.1391(1) Created a Contract.

The Court of Appeals cited three cases that set forth the criteria for determining whether a statute creates a contract. Specifically, the Court stated that a statutory contract arises "only if the Legislature has unambiguously expressed an intention to create the obligation"; that the statute must not be susceptible of any other "reasonable construction than that the Legislature intended to be bound by a contract"; and that the statutory language must demonstrate a "clear expression of legislative intent to create private rights of a contractual nature enforceable against the state." *Studier*, 260 Mich App at 475-476. However, the Court did not apply these principles to the language in MCL 38.1391(1). *Id.* Instead, the Court of Appeals simply concluded, without analysis, that MCL 38.1391(1) demonstrated a legislative intent to create a contract:

[T]he language of MCL 38.1391(1) demonstrates a clear expression of legislative intent to create contractual rights for public school employees. [footnote deleted] Health insurance is part of an employee's benefit package and the whole package is an element of consideration that the State contracts to tender in exchange for services rendered by the employees. [*Studier*, 260 Mich App at 476.]

The conclusion of the Court of Appeals is erroneous because it failed to apply the principles that determine when a statute creates a contract.

E. The Court of Appeals decision raises the specter that other statutes that use the word "shall" might be construed to create a contract.

A possible inference from the Court of Appeals decision is that the language in MCL 38.1391(1), i.e., the statement that the retirement system "shall" pay the premium, imposes a contractual obligation upon Defendants. If this language determines whether there is a contract, then other statutes that contain the word "shall" might also be construed as creating a contract. For example, MCL 38.20d(1) provides that the State Employees' Retirement Board "shall" pay

health care premiums for state retirees under authorized plans. MCL 38.1642(1) provides that the State Police Retirement System "shall" pay health benefit premiums for its retirees under authorized plans. MCL 38.1050b provides that the Legislative Retirement System "shall" pay the premium for hospitalization and medical insurance coverage. MCL 38.68(4) and MCL 38.1079(4) provide that the State "shall" pay for health care benefits for certain former qualified participants in the State Employees' Retirement System and the Legislative Retirement System who elect coverage in authorized health plans.<sup>20</sup>

Under the Court of Appeals' decision, each of these provisions could conceivably be construed as creating a contract. If so, the Legislature could not amend these statutory provisions even if the State did not have the funds necessary to make the required payments. Clearly, the Legislature never intended these statutes to create contracts, and the Court of Appeals erred to the extent it concluded otherwise. At most this language creates a statutory obligation to pay the premium of whatever health care plan the system might adopt, and it is undisputed that the system has paid the necessary premiums and satisfied this obligation. That statutory language is subject to legislative amendment; it does not create any contractual right to particular deductibles or co-pays.

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<sup>20</sup> Numerous other statutes provide that payment "shall" be made. For example, MCL 38.9 provides that the state treasurer "shall" pay disbursements from retirement system funds upon vouchers authorized by the State Employees' Retirement Board. According to MCL 38.11(6), income, interest and dividends derived from deposits and investments authorized by the State Employees' Retirement Act "shall" be paid into an income fund. MCL 41.75 states that payment of approved claims authorized by a township board "shall" be paid by the township treasurer, and MCL 41.289 provides that the expense of lighting of highways and bridges "shall" be paid out of township funds where the township board authorized the expenditure of such funds. MCL 46.175 states that the county agency of a unit of government may enter into agreements whereby the unit "shall" pay the county for the services provided by any improvements and facilities authorized by the county public improvement act. MCL 247.660e provides that the state transportation department "shall" pay up to 80% of the non-reimbursable cost for intercity passenger operating assistance projects authorized by the state transportation commission.

In summary, if this Court concludes that the word "shall" in MCL 38.1391(1) creates a contract, then its decision could be used as precedent to argue that a multitude of other statutes that direct the State to do something by using the word "shall" also create contracts. Such a holding would be contrary to the intent of the Legislature, usurp the sovereign powers of future Legislatures, and create a financial nightmare for the State.

## **CONCLUSION**

MCL 38.1391(1) does not create a contractual obligation for health benefits for retirees of MPERS. The Legislature did not intend to create a contract when it enacted MCL 38.1391(1). It did not include words typically included when a contract is intended or created such as "contract," "agreement," "promise," or "covenant." Moreover, if the Legislature had intended to create a contract it would have required the creation of a Plan rather than giving the Board and the Department the discretion to do so. Furthermore, if the Legislature had intended to create a contract, it would have included language in MCL 38.1391(1) that could not be amended. Finally, the Legislature did not create a contract because it would have required giving up its sovereign authority to appropriate limited tax revenues, and would have bound the Legislature to make payments for retiree health benefits forever.

In summary, MCL 38.1391(1) is simply a declaration of a legislative policy to be pursued. That policy may be modified as medical advances occur, health benefit costs change and the State's revenues change.

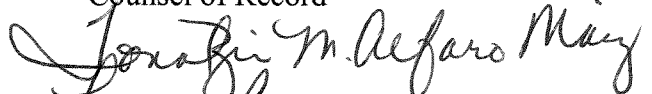

**RELIEF SOUGHT**

The Defendants-Appellants request this Court to reverse that portion of the Court of Appeals' decision that held that MCL 38.1391(1) created contractual rights for public school employees and retirees and affirm the remainder of that decision.

Respectfully submitted,

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